



Company report

AmInvestment Bank

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HARTEALEGA HOLDINGS

(HART MK EQUITY, HTHB.KL)

4 Aug 2021

Best-ever quarterly earnings but tough road ahead

HOLD

(Maintained)

Rationale for report: Company results/update

Price	RM6.80
Fair Value	RM6.87
52-week High/Low	RM21.16/RM6.64

Key Changes

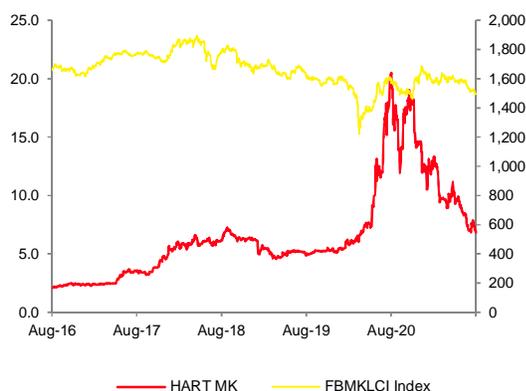
Fair value	↕
EPS	↕

YE to Mar	FY21	FY22F	FY23F	FY24F
Revenue (RM mil)	6,703.5	9,596.9	6,810.4	6,176.5
Core net profit (RM mil)	2,885.4	4,466.1	1,519.0	903.7
FD Core EPS (sen)	84.4	130.7	44.4	26.4
FD Core EPS growth (%)	565.4	54.8	(66.0)	(40.5)
Consensus Net Profit (RM mil)	-	3,832.0	1,845.0	1,269.0
DPS (sen)	51.0	78.0	27.0	16.0
PE (x)	8.1	5.2	15.3	25.7
EV/EBITDA (x)	5.3	3.5	9.1	13.7
Div yield (%)	7.5	11.5	4.0	2.4
ROE (%)	76.8	76.0	21.5	11.9
Net Gearing (%)	nm	nm	nm	nm

Stock and Financial Data

Shares Outstanding (million)	3,417.5
Market Cap (RM mil)	23,238.8
Book Value (RM/share)	1.46
P/BV (x)	4.6
ROE (%)	76.8
Net Gearing (%)	-
Major Shareholders	Hartalega Industries S/B (47.9%) KWAP (3.0%) Kuan Kam Peng (1.8%)
Free Float	1,010.9
Avg Daily Value (RM mil)	49.9

Price performance	3mth	6mth	12mth
Absolute (%)	(31.9)	(48.4)	(66.8)
Relative (%)	(27.8)	(45.6)	(65.2)



Investment Highlights

- We maintain our **HOLD** call on Hartalega Holdings (Hartalega) with an unchanged fair value of RM6.87/share, reflecting a 3% premium for an ESG rating of four stars. Our valuation is based on an unchanged PER of 15x FY23F FD EPS.
- Hartalega's 1QFY22 net profit of RM2.26bil came in within our forecasts but above consensus, accounting for 51% and 59% of full-year expectations respectively. For the quarter, the group boasted a strong utilisation rate of 96% alongside its highest ever quarterly blended glove average selling price (ASP).
- We maintain our earnings forecasts as we expect the group to post weaker results in the remaining quarters, even after factoring in Delta variant-driven demand. This is due to a combination of production disruption, falling ASP, loss of market share and lack of visibility concerning post-pandemic demand-supply dynamics.
- Ultimately, a sharply weakening investor sentiment is expected to keep a lid on its share price in the next six months, despite attractive valuations. Local players are currently trading at PE ratios of 13–18x FY22F EPS, in comparison to pre-pandemic values in the >20x range.

Financial results

- The group reported its best ever quarterly revenue of RM3.9bil (+70% QoQ, 3.2x YoY) due to strong ASP and utilisation rate of 96%. Excluding contribution from shipment delays from March, the utilisation rate would have been 88%. Hartalega's quarterly ASP experienced a 13% QoQ growth to US\$94/1,000 pcs in 1QFY22.
- The group reported an improved PBT margin of 74.7% (+8.1ppt QoQ, +43.9ppt YoY) in 1QFY22. This was due to the higher sales volume, as well as the COGS for orders delayed to 1QFY22 (as result of shipping constraints) being included in the past quarter's results. Going forward, nitrile rubber prices are expected to fall as result of oversupply.
- The group does not normally announce dividends for its first quarter. We are expecting a payout ratio of 60% for FY22F.

Outlook

- **Following yesterday's result briefing, here are our opinions on Hartalega's outlook:**

1. **ASP to trend downwards following encouraging global vaccination rates.** The group expects a 30% QoQ decline in ASP in 2QFY22 (~US\$66/1,000 pcs). Following the trend of market prices, we believe that Hartalega's ASP may drop to an average of US\$40–45/1,000 pcs by 3QFY22. The group is expecting nitrile gloves to be priced at US\$30–35/1,000 pcs post-pandemic. This is in line with our projections.

We are expecting glove players to revert to cost-plus pricing post-pandemic, with lacklustre global demand affecting the spot market. Already, customers have achieved a form of bargaining power by maintaining low inventory levels of one to three months, as they adopt a wait-and-see-approach amid a backdrop of ASP falling on a monthly basis.

2. **Production disruptions to continue.** We expect Hartalega to report a 60% utilisation rate in the following quarter. Factories are currently performing at 70% utilisation rate under MCO 60% workforce restrictions. This is further exacerbated by the EMCO, which resulted in >95% of production being closed for two weeks.

However, a high vaccination rate amongst workers may provide some upside risk. Currently, 90% of workers have received their first dose. The group expects to complete the second dose for 100% of workers by August. Having done so, the group will appeal to remove its 60% workforce restrictions.

3. **Loss of market share to China companies.** Frequent production disruptions have affected the reliability of Malaysian glove producers in the eyes of US and other global customers. Some customers have turned to China producers to fulfil demand, opting to multi-source as a form of risk mitigation. In light of this setback, Hartalega predicts that it may take 2 years to regain consumer confidence. The group believes that it may not be able to fully utilise its production capacity for at least one year.

4. **Lack of visibility concerning post-pandemic supply-demand dynamics may delay expansion plans. The group expects other local glove players to face a similar predicament.** Hartalega cited difficulties in predicting post-pandemic rubber glove demand, although it believes that demand in 2021F will be far lower than MARGMA's forecast of 500bil pcs.

Thus, the status of the four remaining plants in NGC1.5 and 16 plants to be built in Kedah remains unknown. The group currently has a total annual production of 42bil pcs. Plants 8–11 of NGC1.5 are expected to bump up production by 19bil pcs, with the first line's commencement delayed to 1Q2022 from 4Q2021.

5. Although **ESG issues** are plaguing the industry, **we do not expect Hartalega to experience major setbacks**, especially for the upcoming NHS contract negotiations. The group has made some significant progress in resolving major forced labour issues (even prior to the pandemic) and our 4-star rating reflects this.

EXHIBIT 1: FINANCIAL RESULTS

YE to Mar	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	QoQ %	YoY %
Revenue	920.1	1,346.0	2,129.9	2,299.9	3,902.8	69.7%	324.2%
EBIT	273.8	685.5	1,343.6	1,511.4	2,878.3	90.4%	951.4%
Pretax profit	272.8	683.0	1,345.9	1,511.8	2,879.1	90.4%	955.3%
Taxation	(51.8)	(133.3)	(338.0)	(386.7)	(616.8)	59.5%	1091.7%
Minority Interest	(1.3)	(4.7)	(6.2)	(6.0)	(2.7)	-54.4%	103.5%
Net Profit	219.7	545.0	1,001.6	1,119.1	2,259.5	101.9%	928.4%
EPS (sen)	6.4	15.9	29.3	32.7	66.1	101.9%	928.4%
Net gearing (x)	net cash	net cash	net cash	net cash	net cash		
EBIT margin (%)	29.8%	50.9%	63.1%	65.7%	73.7%		
PBT margin (%)	29.7%	50.7%	63.2%	65.7%	73.8%		
Net profit margin (%)	23.9%	40.5%	47.0%	48.7%	57.9%		
Effective tax rate (%)	19.0%	19.5%	25.1%	25.6%	21.4%		

Source: Hartalega, AmInvestment Bank Bhd

EXHIBIT 2: PB BAND CHART



EXHIBIT 3: PE BAND CHART



EXHIBIT 4: ESG MATRIX

Overall	★	★	★	★	
Water + energy conservation	★	★	★		
Pollution + waste regulation	★	★	★		
Sustainable sourcing	★	★	★		
Occupational safety + health	★	★	★	★	★
Workplace diversity	★	★	★		
Employee training + wellbeing	★	★	★	★	★
Volunteering + charitable giving	★	★	★	★	
Corruption-free pledge	★	★	★		
Accessibility & transparency	★	★	★	★	

We accord a discount/premium of -6%, -3%, 0%, +3% and +6% on fundamental fair value based on the overall ESG rating as appraised by us, from 1-star to 5-stars.

Source: AmInvestment Bank Bhd

EXHIBIT 5: FINANCIAL DATA

Income Statement (RMmil, YE 31 Mar)	FY20	FY21	FY22F	FY23F	FY24F
Revenue	2,924.3	6,703.5	9,596.9	6,810.4	6,176.5
EBITDA	688.5	3,952.1	5,869.1	2,127.6	1,371.3
Depreciation/Amortisation	(125.3)	(137.8)	(162.0)	(182.7)	(204.1)
Operating income (EBIT)	563.1	3,814.3	5,707.1	1,944.9	1,167.2
Other income & associates	-	-	-	-	-
Net interest	(7.7)	(0.9)	0.1	4.8	(0.6)
Exceptional items	-	-	-	-	-
Pretax profit	555.4	3,813.4	5,713.2	1,959.7	1,176.6
Taxation	(121.0)	(909.8)	(1,228.3)	(421.3)	(253.0)
Minorities/pref dividends	(0.8)	(18.2)	(18.8)	(19.4)	(19.9)
Net profit	433.6	2,885.4	4,466.1	1,519.0	903.7
Core net profit	433.6	2,885.4	4,466.1	1,519.0	903.7
Balance Sheet (RMmil, YE 31 Mar)	FY20	FY21	FY22F	FY23F	FY24F
Fixed assets	2,002.2	2,156.4	2,267.7	2,502.6	2,728.5
Intangible assets	28.8	32.6	32.6	32.6	32.6
Other long-term assets	194.4	260.7	1,000.0	1,400.0	1,470.0
Total non-current assets	2,225.4	2,449.7	3,300.3	3,935.2	4,231.1
Cash & equivalent	305.2	2,668.7	3,387.6	4,422.9	4,684.0
Stock	273.9	646.7	925.9	657.0	760.1
Trade debtors	502.1	929.9	1,331.3	944.7	1,092.9
Other current assets	7.4	137.0	137.0	137.0	137.0
Total current assets	1,088.5	4,382.4	5,781.8	6,161.7	6,674.0
Trade creditors	273.9	1,059.3	1,515.7	1,903.9	2,512.6
Short-term borrowings	85.4	103.5	260.9	288.7	50.1
Other current liabilities	47.7	230.6	230.6	230.6	230.6
Total current liabilities	407.0	1,393.4	2,007.2	2,423.2	2,793.2
Long-term borrowings	188.6	239.5	239.5	239.5	239.5
Other long-term liabilities	175.2	200.1	50.0	50.0	50.0
Total long-term liabilities	363.8	439.6	289.5	289.5	289.5
Shareholders' funds	2,539.8	4,974.8	6,775.2	7,371.5	7,806.7
Minority interests	3.3	24.2	10.1	12.5	15.6
BV/share (RM)	0.74	1.46	1.99	2.16	2.29
Cash Flow (RMmil, YE 31 Mar)	FY20	FY21	FY22F	FY23F	FY24F
Pretax profit	555.4	3,813.4	5,713.2	1,959.7	1,176.6
Depreciation/Amortisation	125.3	137.8	162.0	182.7	204.1
Net change in working capital	932.0	(473.9)	(292.3)	1,264.0	160.1
Others	(957.0)	(389.6)	(2,724.9)	(2,444.0)	(878.3)
Cash flow from operations	655.7	3,087.7	2,858.1	962.5	662.5
Capital expenditure	(251.3)	(251.3)	(400.0)	(412.0)	(424.4)
Net investments & sale of fixed assets	-	-	-	-	-
Others	6.4	(94.1)	365.0	400.0	70.0
Cash flow from investing	(244.9)	(345.4)	(35.0)	(12.0)	(354.4)
Debt raised/(repaid)	(88.3)	97.1	561.5	1,007.5	499.7
Equity raised/(repaid)	84.0	154.1	-	-	-
Dividends paid	(249.0)	(604.2)	(2,665.6)	(922.7)	(546.8)
Others	(12.2)	(31.6)	-	-	-
Cash flow from financing	(265.4)	(384.6)	(2,104.2)	84.8	(47.1)
Net cash flow	145.4	2,357.6	718.9	1,035.3	261.1
Net cash/(debt) b/f	150.4	305.2	2,668.7	3,387.6	4,422.9
Net cash/(debt) c/f	305.2	2,668.7	3,387.6	4,422.9	4,684.0
Key Ratios (YE 31 Mar)	FY20	FY21	FY22F	FY23F	FY24F
Revenue growth (%)	3.4	129.2	43.2	(29.0)	(9.3)
EBITDA growth (%)	4.0	474.0	48.5	(63.7)	(35.5)
Pretax margin (%)	19.0	56.9	59.5	28.8	19.1
Net profit margin (%)	14.8	43.0	46.5	22.3	14.6
Interest cover (x)	73.0	4,384.3	nm	nm	2,078.3
Effective tax rate (%)	21.8	23.9	21.5	21.5	21.5
Dividend payout (%)	63.1	60.4	59.7	60.7	60.5
Debtors turnover (days)	60	39	43	61	60
Stock turnover (days)	34	25	30	42	42
Creditors turnover (days)	33	36	49	92	130

Source: Company, AmInvestment Bank Bhd estimates

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